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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. —

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

WILLIAM D. DISTON

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Third Circuit entered in this case.

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 60-63) and the opinion of the Circuit Court of Appeals (R. 72-79) have not been reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 12, 1944 (R. 79). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether gifts in trust for taxpayer's minor children were gifts of future interests within Section 504 (b) of the Revenue Act of 1932, and hence to be included in taxpayer's net gifts.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 502. COMPUTATION OF TAX.

The tax for each calendar year shall be an amount equal to the excess of—

(1) a tax, computed in accordance with the Rate Schedule hereinafter set forth, on the aggregate sum of the net gifts for such calendar year and for each of the preceding calendar years, over

(2) a tax, computed in accordance with the Rate Schedule, on the aggregate sum of the net gifts for each of the preceding calendar years.

SEC. 504. NET GIFTS.

(a) *General Definition.*—The term "net gifts" means the total amount of gifts made during the calendar year, less the deductions provided in section 505.

(b) *Gifts Less Than \$5,000.*—In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first \$5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included

in the total amount of gifts made during such year.

Treasury Regulations 79 (1936 ed.):

ART. 9. *Net gifts.*—The tax is computed upon the amount of the donor's net gifts (see articles 5, 6, and 7). The term "net gifts" means the "total amount of gifts" computed as provided in section 504 (see article 10), less the deductions provided in section 505. (See articles 12 and 13.)

ART. 11. *Future interests in property.*—No part of the value of a gift of a future interest may be excluded in determining the total amount of gifts made during the calendar year. "Future interests" is a legal term, and includes reversions, remainders, and other interests or estates, whether vested or contingent, and whether or not supported by a particular interest or estate, which are limited to commence in use, possession, or enjoyment at some future date or time. * * *

STATEMENT

The facts, as stipulated and found by the Tax Court, are not in dispute. They may be summarized as follows:

By deed dated December 17, 1936, the taxpayer created a trust for the benefit of each of his five children, three of whom were then minors (R. 27). In auditing the taxpayer's gift tax return for

the year 1936, the Commissioner determined that the taxpayer had made gifts in that year to his wife and children in an aggregate amount of \$71,952.49 (R. 27).

The Commissioner allowed the taxpayer an exclusion of \$5,000 on each gift to his five children and on the gift to his wife. The taxpayer's net gifts for the year 1936, after deducting an exemption of \$40,000, were accordingly computed to be \$1,952.49, upon which a tax was duly assessed and paid (R. 28).

On March 21, 1937, the taxpayer augmented the corpus of the trust by transferring to the trustees 500 shares of stock having an aggregate value of \$25,000 (R. 28). Upon receipt of this stock the trustees allocated 100 shares, having a value of \$5,000, to each of the taxpayer's five children, three of whom were still minors (R. 28). On December 9, 1938, the taxpayer created another trust for the benefit of each of his five children, the corpus consisting of two tracts of land worth \$38,581.54 (R. 28). When the 1938 trust was established, two of the taxpayer's children were still minors.

The terms of the two trusts were substantially identical in their provisions for each of the taxpayer's minor children. The trust instrument of December 17, 1936, provided, in part, as follows (R. 29, 31, 33, 34, 36-37):

SECOND. Terms of the Trust: Trustees shall divide the principal of the trust into five equal shares and shall hold, manage, invest and reinvest the principal of said shares in accordance with the powers hereinafter granted, **IN TRUST, NEVERTHELESS,** as follows:

* * * * *

3. As to the third of said equal shares of principal, to accumulate the net income therefrom for the benefit of **WILLIAM L. DISSTON** until he reaches the age of twenty-one years, at which time to pay over to him all accumulated income, and thereafter to pay over to him in not less than quarterly instalments the entire net income derived therefrom during his lifetime; provided, however, that upon his reaching the age of forty-five years one-half of the principal of his share shall be paid over to him free and discharged of all trusts; * * * *

* * * * *

6. Trustees shall hold the shares of minors in whom the principal shall have vested during their respective minorities, and during such time shall apply such income therefrom as may be necessary for the education, comfort and support of the respective minors, and shall accumulate for each minor until he or she reaches the age of twenty-one years, all income not so needed. The foregoing clause shall apply to minor children of the Settlor irrespective of the direction heretofore set forth to

accumulate all income for such minors. In the administration of the shares of the minors, the Trustees shall have all of the powers, duties and discretions, including the power of investment and reinvestment, as are conferred upon them as Trustees hereunder.

FOURTH. Trustees' Powers: . . .

7. To apply the income to which any beneficiary shall be entitled hereunder for the maintenance, education and support of such beneficiary should he or she by reason of age, illness or any other cause in the opinion of the Trustees be incapable of dispensing it. Payment by the Trustees to the parent of any minor or to the person with whom such minor resides and the receipt of such parent or such person shall be sufficient acquittance and discharge to the Trustees for such payment or payments.

Partial payments of income from the 1936 trust were made to the parent of the minor beneficiaries in each of the years 1936, 1937, and 1938 (R. 56-58). At the time the case was before the Tax Court, there had been no net income from the 1938 trust (R. 59). In 1937, checks representing trust income were sent by the corporate trustee to the mother of the then minor beneficiaries, but she returned them with instructions to accumulate and hold the income until the children became of

age (R. 57-59). The third child became of age April 12, 1938 (R. 57). After 1937 the trust income for the fourth child was accumulated until she became of age (R. 59). Since 1937 the trust income for the youngest child has been accumulated (R. 59).

In determining the taxpayer's gift tax for the year 1937, the Commissioner disallowed three \$5,000 exclusions from taxpayer's net gifts for that year on the ground that the gifts to the three minor children were gifts of future interests (R. 8-9). For the year 1938, the Commissioner disallowed two \$5,000 exclusions from taxpayer's net gifts for that year on the ground that the gifts to the two children who were still minors were gifts of future interests (R. 21).

The Tax Court upheld the Commissioner's determinations (R. 63), but its decision was reversed by the Circuit Court of Appeals for the Third Circuit, sitting *en banc* (R. 79). Judge Biggs dissented. In so holding the court below expressly overruled its prior decision in *Commissioner v. Taylor*, 122 F. 2d 714, certiorari denied, 314 U. S. 699.

For the purpose of determining the taxpayer's net gifts in prior years the Commissioner adjusted the exclusions which had been allowed for the gifts to the minor children in 1937 (R. 9). At the time this adjustment was made the year 1936 was closed by the statute of limitations (R. 63).

The Tax Court also upheld the Commissioner's determination in this respect (R. 63). In view of its conclusion regarding the principal question, however, the court below did not pass on this question.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred in holding that the gifts to taxpayer's minor children were not gifts of future interests within the meaning of Section 504 (b) of the Revenue Act of 1932, and in reversing the decision of the Tax Court.

REASONS FOR GRANTING THE WRIT

1. The decision below is directly in conflict with rulings of the Circuit Courts of Appeals for the First, Fifth, and Eighth Circuits. *Welch v. Paine*, 120 F. 2d 141 (C. C. A. 1st); *Welch v. Paine*, 130 F. 2d 990 (C. C. A. 1st); *Fondren v. Commissioner*, 141 F. 2d 419 (C. C. A. 5th), in which certiorari was granted October 9, 1944, No. 88, this Term; *French v. Commissioner*, 138 F. 2d 254 (C. C. A. 8th). These cases hold that where income is to be accumulated for a beneficiary during his minority and the trustee is directed to or has discretion to apply so much of the income as may be necessary for the education and support of the minor beneficiary, the gift is one of a future interest. The holding of the court below is also inconsistent in principle with *Commissioner v. Gardner*, 127 F. 2d 929 (C. C. A. 7th).

2. The construction of the statute made by the court below is contrary to the interpretation embodied in Articles 9 and 11 of Treasury Regulations 79 (1936 ed.), *supra*. The lower court held that where income is to be accumulated for a minor beneficiary, the donor has made as complete a gift as is possible, and that Congress did not intend to discriminate against such gifts merely because the legal disability of the beneficiary prevented present distributions of income. The minority of a beneficiary does not require, however, that his share of the income be accumulated by the trust. See *Fisher v. Commissioner*, 132 F. 2d 383 (C. C. A. 9th); and *Kinney v. Anglim*, 43 F. Supp. 431 (N. D. Cal.), appeal dismissed on stipulation, 127 F. 2d 291 (C. C. A. 9th), where the trustees were to pay the income to the parents of the minor beneficiaries and the gifts of income were treated as present gifts. In any event, when a donor has made a gift in a particular manner, the nature of the donee's interest under the statute is not dependent upon whether the donor was restricted in his choice of selecting the method by which the gifts should be made. There is no indication that Congress intended to adopt such a criterion of a future interest. See H. Rep. No. 708, 72d Cong., 1st Sess., p. 29 (1939-1 Cum. Bull. (Part 2) 457, 478); S. Rep. No. 665, 72d Cong., 1st Sess., p. 41 (1939-1 Cum. Bull. (Part 2) 496, 526), with respect to the reasons for excluding

gifts of future interests from the exemption. The minor beneficiaries in this case do not have present possession or enjoyment of the complete value of the gift made to them. Since their possession or enjoyment will commence only at a future date, we submit that their interests are future interests within the meaning of the statute.

3. The question presented is important in the administration of the law. Section 1003 (b) (3) of the Internal Revenue Code, as amended by Section 454 of the Revenue Act of 1942, c. 619, 56 Stat. 798 (26 U. S. C. 1940 ed., Supp. III, Sec. 1003), excludes gifts of future interests in property from the \$3,000 exemption provided for gifts made during 1943 and subsequent years. Consequently, the problem is likely to recur. The decision below, as pointed out in the dissenting opinion of Judge Biggs, may give rise to serious problems in evaluating the interest of the beneficiary.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

OCTOBER 1944.

